

AUDIT COMMITTEE REPORT

COMPOSITION OF THE AUDIT COMMITTEE

The Board Audit Committee comprises of three Non-Executive Directors of the Bank, majority of whom are independent. The following Directors functioned on the Audit Committee during 2010, viz.:

Members	Status	Committee Member Since	Attendance at Meetings in 2010 (Attended/ Eligible to Attend)
Mr. Lalith Withana <i>(Chairman)</i>	Independent Non-Executive Director	5th January 2009	6/6
Mr. Nihal Jayamanne PC	Senior Independent Non-Executive Director	24th February 2009	6/6
Mr. P.G.S. Kariyawasam <i>(resigned w.e.f. 14th May 2010)</i>	Non-Executive Director	3rd December 2009	1/2
Mr. P. Kudabalage <i>(appointed w.e.f. 31st August 2010)</i>	Non-Executive Director	31st August 2010	1/2

The Chairman of the Committee is Mr. Lalith Withana, who is an Independent Non-Executive Director and a Fellow of The Institute of Chartered Accountants of Sri Lanka and Fellow of the Chartered Institute of Management Accountants, U.K. Mr. P. Kudabalage who replaced Mr. P.G.S. Kariyawasam on the Audit Committee is also a Fellow of The Institute of Chartered Accountants of Sri Lanka and the Institute of Certified Management Accountants of Sri Lanka.

The Executive Director Mr. R. Nadarajah, Chief Executive Officer, Chief Financial Officer and Deputy General Manager Internal Audit attend Audit Committee meetings by invitation. The External Auditors attend the meetings whenever the Committee requires their presence. The Company Secretary functions as the Secretary to the Audit Committee.

MEETINGS

As per the Audit Committee Charter, the Committee is required to meet at least 4 times a year. However, during the year under review, the Committee met 6 times and reports of internal and external audits were discussed at these meetings. The Minutes of the Committee were made available to the Board of Directors for information and necessary action.

TERMS OF REFERENCE

The Audit Committee functions within its board-approved terms of reference also referred to as the Audit Committee Charter. It also ensures that its role, composition and responsibilities comply with International Best Practices and Corporate Governance Rules as laid down in Section 3 (6) (ii) of the Banking Act Direction No. 11 of 2007, titled 'Corporate Governance for Licensed Commercial Banks in Sri Lanka' and subsequent amendments thereto, Rule 7.10.6 of the Listing Rules of the Colombo Stock Exchange and the Code of Best Practice on Corporate Governance jointly issued by the Securities & Exchange Commission of Sri Lanka (SEC) and The Institute of Chartered Accountants of Sri Lanka (ICASL). The Committee also adopted the Guidelines issued by The Institute of Chartered Accountants of Sri Lanka (ICASL) around end December 2010 on the determination of effectiveness of the internal control mechanism.

MAIN RESPONSIBILITIES

The main objective of the Audit Committee is to assist the Board of Directors to effectively carry out its responsibilities relating to financials and

other connected affairs of the Bank. The main responsibilities include -

1. Reviewing and monitoring the integrity of the Financial Statements, financial reporting, information databases and audit process.
2. Examining any matter relating to financial and other connected affairs of the Bank.
3. Monitor all internal and external audits and inspection programmes.
4. Review and take action on all internal and external audit reports and follow-up on the recommendations.
5. Review and monitor IT governance activities.
6. Review and monitor the systems of internal controls.
7. Review and monitor the system for approval and monitoring of expenses including capital expenditure.
8. Review and monitor statutory and regulatory compliance process.
9. Approving the annual internal audit plans.
10. Review Bank's annual accounts and interim Financial Statements.
11. Review the process of carrying investigations wherever necessary to assist the Board.

ACTIVITIES DURING THE YEAR

Committee carried out the following activities during the year under review:

Internal Audit Charter

To further strengthen the internal audit function and structure, an Internal Audit Charter was prepared and approved during 2010 in addition to the Board Audit Committee Charter that was approved in 2009.

The Internal Audit Charter consisted factors such as scope, functions, authority, responsibility, adjudication, external relationship management and ethics, that ably assist and direct/guide the Internal Audit Department to discharge its functions independently.

Financial Reporting

The Committee discussed and reviewed the financial reporting process in the Bank on behalf of the Board. All interim Financial Statements and annual Financial Statements were reviewed prior to their release for compliance with statutory and regulatory requirements including the Sri Lanka Accounting Standards, the Companies Act No. 7 of 2007, Sri Lanka Accounting and Auditing Standards Act No. 15 of 1995, the Banking Act No. 30 of 1988 (as amended). Conformity was also ensured to other regulatory requirements such as the Listing Rules of the Colombo Stock Exchange and Banking Act Direction No. 11 of 2007 and subsequent amendments thereto.

Regulatory Compliance

Procedures were in place to ensure compliance with banking and other statutory regulations. During the year, these procedures were reviewed through monthly/quarterly reports submitted by the senior management to the Board of Directors.

Internal Audit and Inspection

The Committee approved the Internal Audit plan for 2010 and monitored its status throughout the year. A total of 54 audits and 115 investigations were carried out. The Committee reviews and monitors the effectiveness of the internal audit and inspection functions and the performance of the Internal Audit and Inspection Department. Special training programmes were designed and conducted during the year to upgrade the competence levels required on information system audits and investigation in addition to the internal and external training programmes.

External Audit

The Committee met with the External Auditors - KPMG - Ford, Rhodes, Thornton & Co., during the year on to discuss the Management Letter in respect of the year 2009, Audited Financial Statements for 2009 and also to plan out the scope, approach and the methodology to be adopted in carrying out of the annual audit for 2010.

The Audit Committee reviewed the Non-Audit Services provided by the External Auditor and was of the view that such services were not within the category of services identified as restricted under the guidelines issued by the Central Bank of Sri Lanka, for External Auditors, relating to their statutory duties in terms of Section 39 of the Banking Act No. 30 of 1988 and as amended by Banking Act No. 33 of 1995.

Audit Manual

Upon the Committee's recommendation, the Board approved the adoption of a risk-based Internal Audit Manual, which was outsourced to PricewaterhouseCoopers, Chartered Accountants.

Governance

The Committee also ensured that good corporate governance was practiced in conformity with the Banking Act Direction No. 11 of 2007 and subsequent amendments thereto (Central Bank Code of Corporate Governance for licensed commercial banks), the Listing Rules of the Colombo Stock Exchange and the Code of Best Practice on Corporate Governance issued jointly by the SEC & ICASL and appropriate procedures were in place to conduct independent investigations whenever it was needed.

System of Internal Controls

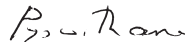
The Committee also reviewed the effectiveness of the Bank's internal controls over financial reporting and other controls relating to core areas such as deposit accepting, credit approval, operations, compliance and risk management systems as per the Guidelines issued by The Institute of Chartered Accountants of Sri Lanka (ICASL). The Board's statement on the effectiveness of the Bank's internal control mechanism, as reviewed by the Committee is found on pages 111 and 112 of this Annual Report.

In accordance with Sri Lanka Standard on Assurance Engagements SLSAE 3050 - Assurance Report for Banks on Directors' Statement on Internal Control, External Auditor's have issued an Independent Assurance Report on the Bank's internal control mechanism.

Evaluation of the Committee

As authorised by the Board, the Integrated Risk Management Subcommittee of the Board through an annual evaluation assessed the effectiveness of the Audit Committee as satisfactory.

The Audit Committee has recommended to the Board of Directors that Messers KPMG Ford, Rhodes, Thornton & Co., be reappointed as Auditors for the financial year ending 31st December 2011, subject to the approval of shareholders at the next Annual General Meeting.



Lalith Withana

Chairman - Audit Committee

18th February 2011

INTEGRATED RISK MANAGEMENT COMMITTEE REPORT

The Integrated Risk Management Committee appointed by the Board comprises of three Non-Executive Directors, one of whom is independent.

The following Directors functioned on the Committee during 2010, viz.:

Members	Status	Committee Member Since	Attendance at Meetings in 2010 (Attended/Eligible to Attend)
Mr. Ajith Devasurendra (<i>Chairman</i>)	Non-Executive Director	3rd December 2009	5/6
Mr. Lalith Withana	Independent Non-Executive Director	5th January 2009	6/6
Mr. P.G.S. Kariyawasam (<i>resigned on 14th May 2010</i>)	Non-Executive Director	3rd December 2009	1/2
Mr. A.M.M. de Alwis (<i>appointed w.e.f. 31st August 2010</i>)	Non-Executive Director	31st August 2010	2/3

The Committee is headed by a Non-Executive Chairman, Mr. A.L. Devasurendra. Mr. A.M.M. de Alwis was appointed to the Committee on 31st August 2010 upon the resignation of Mr. P.G.S. Kariyawasam. Brief profiles of the members are given on pages 314 to 317 of this Annual Report. The Company Secretary functions as the Secretary of the Committee.

The Executive Director Mr. Nadarajah, the CEO, Chief Risk Officer, Chief Financial Officer and Key Management Personnel, supervising broad risk categories, i.e., credit, market, liquidity, operational and strategic risks attend the Committee meetings by invitation.

The Committee is responsible for the following:

- to ensure, that a risk management framework is in place to facilitate proactive risk management and oversight of overall control environment
- set risk management policy, strategy, procedures and policy controls and systems and test the effectiveness of such policies using measurement tools.
- assess all risks, i.e., credit, market, liquidity, operational and strategic risks to the Bank through appropriate risk indicators and management information and periodically review the risk exposures of the Bank in line with risk management strategies and objectives and also set risk concentration limits in line with the Bank's risk appetite.

- mitigate specific risks which are above prudent levels decided by the Committee and establish risk tolerance at enterprise and strategic business unit levels.
- submit risk assessment report within a week of each meeting to the Board, seeking the Board's views, concurrence and/or specific directions.
- establish a compliance function to assess the Bank's compliance with laws, regulations, regulatory guidelines, internal controls and approved policies on all areas of business operations.

The Committee met six times during the year under review. The Minutes of the Committee meeting were made available to the Board of Directors for their information and necessary action and were affirmed by the Board.

EVALUATION OF THE COMMITTEE

As authorised by the Board, the Audit Subcommittee of the Board through an annual evaluation, assessed the effectiveness of the Integrated Risk Management Committee as satisfactory.



Ajith Devasurendra

Chairman - Integrated Risk Management Committee

26th January 2011

HR AND REMUNERATION COMMITTEE REPORT

The HR & Remuneration Committee appointed by the Board comprises of four Non-Executive Directors, three of whom are independent.

The following Directors functioned on the Committee during 2010, viz.:

Members	Status	Committee Member Since	Attendance at Meetings in 2010 (Attended/Eligible to attend)
Mr. Nihal Jayamanne PC (<i>Chairman</i>)	Senior Independent Non-Executive Director	5th January 2009	2/2
Mr. Lalith Withana	Independent Non-Executive Director	5th January 2009	2/2
Rear Admiral (Rtd.) B.A.J.G. Peiris	Independent Non-Executive Director	3rd December 2009	1/2
Mr. P.G.S Kariyawasam <i>(resigned on 14.5.2010)</i>	Non-Executive Director	3rd December 2009	0/0*
Dr. N.H. Godahewa <i>(resigned on 30.6.2010)</i>	Non-Executive Director	3rd December 2009	0/1
Mr. S.P.S Ranatunga <i>(appointed w.e.f. 13th January 2010)</i>	Non-Executive Director	13th January 2010	1/2

* No meetings were held by the Committee up to the date of resignation of Mr. P.G.S. Kariyawasam on 14.5.2010.

The Committee is headed by an independent Non-Executive Chairman, Mr. N.M. Jayamanne PC. Mr. S.P.S. Ranatunga was appointed to the Committee with effect from 13th January 2010. Brief profiles of the members are given on pages 314 and 317 of this Annual Report. The Company Secretary functions as the Secretary of the Committee.

The General Manager/Chief Executive of the Bank is co-opted to the meeting and the Deputy General Manager - Human Resources and Administration and Assistant General Manager - Finance assist the Committee by providing relevant information for their decision making within their Board approved terms of reference.

The Committee met twice during the year under review. The minutes of the committee meetings were made available to the Board of Directors for their information and necessary action and were affirmed by the Board.

REMUNERATION POLICY

The Remuneration Committee is responsible for determining the compensation of the Executive Chairman, Executive Director and other Directors.

Aggregate remuneration paid to Executive and Non-Executive Directors is set out in Note 9 to the Financial Statements.

The Committee also determines the compensation and benefits of the key management personnel including that of the General Manager/Chief Executive based on established performance parameters. In addition to that the Committee is responsible to lay down guidelines and parameters for the compensation structures for all executive staff of the Bank and oversee the implementation of these policies.

The Committee also determines the basis of revising remuneration and other benefits paid.

EVALUATION OF THE COMMITTEE

As authorised by the Board, the Sustainability Subcommittee of the Board through an annual evaluation, assessed the effectiveness of the HR and Remuneration Committee as satisfactory.



Nihal Jayamanne PC

Chairman - Remuneration Committee

26th January 2011

NOMINATION COMMITTEE REPORT

The Nomination Committee appointed by the Board comprises of four Non-Executive Directors two of whom are independent.

The following Directors functioned on the Nomination Committee during 2010, viz.:

Members	Status	Committee Member Since	Attendance at Meetings in 2010 (Attended/Eligible to Attend)
Rear Admiral (Rtd.) B.A.J.G. Peiris <i>(Chairman)</i>	Independent Non-Executive Director	12th January 2009	6/7
Mr. Nihal Jayamanne PC	Senior Independent Non-Executive Director	5th January 2009	7/7
Mr. A.L. Devasurendra	Non-Executive Director	3rd December 2009	6/7
Mr. S.P.S. Ranatunga <i>[appointed w.e.f. 13th January 2010]</i>	Non-Executive Director	13th January 2010	7/7
Mr. Lalith Withana <i>[appointed w.e.f. 9th December 2010]</i>	Independent Non-Executive Director	9th December 2010	(overseas) 0/3*

* All three meetings were held in December 2010 during which period Mr. Withana was overseas.

Mr. S.P.S. Ranatunga was appointed to the Committee with effect from 13th January 2010. Brief profiles of the members of the Committee are given on pages 314 to 317 of this Annual Report. The Company Secretary functions as the Secretary of the Committee. The General Manager/Chief Executive of the Bank and the Executive Directors attended some of the meetings by invitation where succession arrangements, profiling of key management personnel etc. were discussed.

The Nomination Committee is responsible for the following:

- Implementation of procedure to select/appoint new Directors, CEO and key management personnel including review of the structure, size, composition and competencies of the Board from time to time;
- Recommend (or not recommend) the re-election of current Directors having regard to their performance and contribution towards the overall discharge of the Board's responsibilities.

- Establish criteria to determine eligibility for appointment or promotion to the post of CEO and the Key Management positions.
- Ensure that the Directors, CEO and key management personnel are fit and proper persons to hold office as specified in the criteria given in Direction 3(3) of the Banking Act Direction No. 11 of 2007 ('Code of Corporate Governance for Licensed Commercial Banks in Sri Lanka') and subsequent amendments thereto.
- Review and recommend requirements of additional/new expertise and the succession arrangements for retiring Directors and key management personnel from time to time.

The Committee held 7 meetings during 2010. The Committee reviewed the organisation structure of the Bank and identified Key Management handling core areas of the Bank.

The Committee also reviewed the fitness and propriety of Directors, CEO and key management personnel and established a procedure for selection/recruitment/promotion for the CEO and key management personnel.

Bearing in mind that the Board is ultimately responsible for the selection and appointment of Directors, ensuring a balance in its composition of Executive, Non-Executive and Independent Directors, the Nomination Committee reviewed and recommended a policy governing the selection, nomination and election of Directors. This was approved by the Board in July 2010.

EVALUATION OF THE COMMITTEE

As authorised by the Board, the Credit Subcommittee of the Board through an annual evaluation, assessed the effectiveness of the Nomination Committee as satisfactory.



Rear Admiral (Rtd.) B.A.J.G. Peiris

Chairman - Nomination Committee

26th January 2011